

# YES CAPITAL (INDIA) PRIVATE LIMITED

## ASSET-LIABILITY MANAGEMENT POLICY

### REGULATION:

The purpose of this Assets Liability Management Policy ("ALM Policy") is to establish guidelines to ensure prudent management of assets and liabilities for YES Capital (India) Private Limited ("YCPL") ("the Company"). These guidelines address management and reporting of capital, liquidity and interest risk.

The ALM Policy also complies with the requirement of RBI circular DNBS(PD).CC.No.15/02.01/2000-2001 dated 27<sup>th</sup> June, 2001, as amended from time to time.

### BACKGROUND:

1. Intense competition for business involving both the assets and liabilities has brought pressure on the management of CICs to maintain a good balance among spreads, profitability and long-term viability. Imprudent liquidity management can put CICs' earnings and reputation at great risk. These pressures call for structured and comprehensive measures and not just ad hoc action. The managements of CICs have to base their business decisions on a dynamic and integrated risk management system and process, driven by corporate strategy. CICs are exposed to several major risks in the course of their business - credit risk, interest rate risk, equity/commodity price risk, liquidity risk and operational risk. It is, therefore, important that NBFs introduce effective risk management systems that address the issues relating to interest rate and liquidity risks.
2. CICs need to address these risks in a structured manner by upgrading their risk management and adopting more comprehensive Asset-Liability Management (ALM) practices than has been done hitherto. ALM, among other functions, is also concerned with risk management and provides a comprehensive and dynamic framework for measuring, monitoring and managing liquidity and interest rate equity and commodity price risks of major operators in the financial system that needs to be closely integrated with the CICs' business strategy. It involves assessment of various types of risks and altering the asset-liability portfolio in a dynamic way in order to manage risks.
3. Having understood the significance of sound ALM practices, the company proposes to lay down broad guidelines in respect of interest rate and liquidity risks management systems, which form part of the Asset-Liability Management (ALM) function. The initial focus of the ALM function would be to enforce the risk management discipline i.e. managing business after assessing the risks involved. The objective of good risk management systems should be that these systems will evolve into a strategic tool for the company.

4. The ALM process will rest on three pillars:

Pillar	Particulars
ALM Information Systems	<ul style="list-style-type: none"><li>o Management Information Systems</li><li>o Information availability, accuracy, adequacy and expediency</li></ul>
ALM Organization	<ul style="list-style-type: none"><li>o Structure and responsibilities</li><li>o Level of top management involvement</li></ul>
ALM Process	<ul style="list-style-type: none"><li>o Risk parameters</li><li>o Risk identification</li><li>o Risk measurement</li><li>o Risk management</li><li>o Risk policies and tolerance levels</li></ul>



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## 5. ALM Information Systems

- I. ALM has to be supported by a management philosophy which clearly specifies the risk policies and tolerance limits. This framework needs to be built on sound methodology with necessary information systems as back up. Thus, information is the key to the ALM process. There are various methods prevalent world-wide for measuring risks. These range from the simple Gap Statement to extremely sophisticated and data intensive Risk Adjusted Profitability Measurement methods.

However, the central element for the entire ALM exercise is the availability of adequate and accurate information with expedience. Adequate measures will be taken on an ongoing basis to collect accurate data in a timely manner through full scale automation.

## 6. ALM Organization

- I. Successful implementation of the risk management process would require strong commitment on the part of the senior management in the company, to integrate basic operations and strategic decision making with risk management. The Board of Directors will have overall responsibility for management of risks and should decide the risk management policy of the NBFC and set limits for liquidity, interest rate and equity price risks.
- II. The Asset - Liability Committee (ALCO) consisting of the appropriate members will be created in due course and be responsible for ensuring adherence to the limits set by the Board as well as for deciding the business strategy of the company (on the assets and liabilities sides) in line with the company's budget and decided risk management objectives.
- III. The ALM Support Groups consisting of operating staff should be responsible for analyzing, monitoring and reporting the risk profiles to the ALCO. The staff should also prepare forecasts (simulations) showing the effects of various possible changes in market conditions related to the balance sheet and recommend the action needed to adhere to the company's internal limits.
- IV. The ALCO is a decision-making unit responsible for balance sheet planning from risk return perspective including the strategic management of interest rate and liquidity risks. The business and risk management strategy will ensure that the company operates within the limits/parameters set by the Board. The business issues that an ALCO would consider, inter alia, will include product pricing for both deposits and advances, desired maturity profile and mix of the incremental assets and liabilities, prevailing interest rates offered by other peer CICs for the similar services/product, etc. In addition to monitoring the risk levels of the company, the ALCO should review the results of and progress in implementation of the decisions made in the previous meetings. The ALCO would also articulate the current interest rate view of the company and base its decisions for future business strategy on this view. In respect of the funding policy, for instance, its responsibility would be to decide on source and mix of liabilities or sale of assets. Towards this end, it will develop a view on future direction of interest rate movements and decide on funding mixes between fixed vs floating rate funds, wholesale vs retail deposits, money market vs capital market funding, domestic vs foreign currency funding, etc.

Post business commencement, the frequency of holding their ALCO meetings will be Quarterly. However, if the need be for a meeting at a short notice, the ALCO meet at a shorter notice.



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## V. Board of Directors Meetings and Reviews

The Board of Directors, in their board meetings, will oversee the implementation of the system and review its functioning periodically.

## VI. ALM Process

The scope of ALM function can be described as follows:

- a. Liquidity risk management
- b. Management of market risks
- c. Funding and capital planning
- d. Profit planning and growth projection
- e. Forecasting and analysing 'What if scenarios' and preparing contingency plans

The guidelines given in this note mainly address Liquidity and Interest Rate risks.

## 7. Liquidity Risk Management

- I. Measuring and managing liquidity needs are vital for effective operation of any company. The importance of liquidity transcends individual institutions, as liquidity shortfall in one institution can have repercussions on the entire system. ALCO should measure not only the liquidity positions of the company on an ongoing basis but also examine how liquidity requirements are likely to evolve under different assumptions. Experience shows that assets commonly considered as liquid, like Government securities and other money market instruments, could also become illiquid when the market and players are unidirectional. Therefore, liquidity has to be tracked through maturity or cash flow mismatches. For measuring and managing net funding requirements, the use of a maturity ladder and calculation of cumulative surplus or deficit of funds at selected maturity dates is adopted as a standard tool. The format of the Statement of Structural Liquidity as prescribed by Reserve Bank of India (RBI) may be used for this purpose.
- II. The Maturity Profile based on ALM - II could be used for measuring the future cash flows of each company in different time buckets. The time buckets, may be distributed as under:
  - a. 1 day to 30/31 days (One month)
  - b. Over 1 month and up to 2 months
  - c. Over 2 months and up to 3 months
  - d. Over 3 months and up to 6 months
  - e. Over 6 months and up to 1 year
  - f. Over 1 year and up to 3 years
  - g. Over 3 years and up to 5 years
  - h. Over 5 years

As the company does not hold public deposits, all the investment securities would fall in the category of 'non-mandatory securities'. All non-mandatory securities may be kept in buckets of future time frame for the purpose of determining their cash flows based on maturity of such security and intention of holding such security till the time of such maturity.

- III. Alternatively, each company may also follow the concept of Trading Book which is as follows:
  - a. The composition and volume are clearly defined



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- b. Maximum maturity/duration of the portfolio is restricted
- c. The holding period not to exceed 90 days
- d. Cut-loss limit prescribed
- e. Defeasance periods (product-wise) i.e. time taken to liquidate the position on the basis of liquidity in the secondary market is prescribed

Any company maintaining such 'Trading Books' and complying with the above standards may show the trading securities under "1 day to 30/31 days (One month)", "Over one month and up to 2 months" and "Over two months and up to 3 months" buckets on the basis of the defeasance periods. The Board/ALCO of the company should approve the volume, composition, holding/defeasance period, cut loss, etc. of the 'Trading Book'. The remaining investments should also be classified as short-term and long-term investments as required under Prudential Norms.

- IV. The policy note recorded by each company on treatment of the investment portfolio for the purpose of ALM and approved by their Board/ALCO shall be forwarded to the Regional Office of the Department of Non-Banking Supervision of RBI under whose jurisdiction the registered office of the company is located.
  - V. Within each time bucket, there could be mismatches depending on cash inflows and outflows. While the mismatches up to one year would be relevant since these provide early warning signals of impending liquidity problems, the main focus should be on the short-term mismatches viz., 1-30/31 days. Company, however, is expected to monitor its cumulative mismatches (running total) across all time buckets by establishing internal prudential limits with the approval of the ALCO. The mismatches (negative gap) during 1-30/31 days in normal course may not exceed 15% of the cash outflows in this time bucket.
  - VI. The Statement of Structural Liquidity shall be prepared by placing all cash inflows and outflows in the maturity ladder according to the expected timing of cash flows. A maturing liability will be a cash outflow while a maturing asset will be a cash inflow. While determining the likely cash inflows / outflows, company will have to make a number of assumptions according to their asset - liability profiles. While determining the tolerance levels, the company may consider all relevant factors based on their asset-liability base, nature of business, future strategy, etc.
  - VII. In order to enable the company to monitor their short-term liquidity on a dynamic basis over a time horizon spanning from 1 day to 6 months, company will estimate their short-term liquidity profiles based on business projections and other commitments for planning purposes. An indicative format ALM - I issued by RBI for estimating Short-term Dynamic Liquidity will be used for the said purpose.
8. Currency Risk
- CICs does not have any currency risk as of now as there are no transactions entered by any company which will involve currency risk. However, in future, if such transactions are entered, the company in question will take appropriate steps to modify this policy and incorporate measures to check currency risk.



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## 9. Interest Rate Risk (IRR)

The operational flexibility given to NBFCs in pricing most of the assets and liabilities imply the need for the financial system to hedge the Interest rate risk. Interest rate risk is the risk where changes in market interest rates might adversely affect an NBFC's financial condition. The changes in interest rates can affect the company in some way. The immediate impact of changes in interest rates is on earnings (i.e. reported profits) by changing its Net Interest Income (NII). The company will manage this risk on NII by pricing loan products at rates that sufficiently cover interest rate risk. The risk from the earnings perspective can be measured as changes in the Net Interest Income (NII) or Net Interest Margin (NIM). Measurement of such risk will be done at the time of deciding rates to be offered to customers. Once interest rate risk is measured by the ALCO, lending rates of the new loans will be finalized accordingly. The interest sensitive assets and liabilities will be clubbed into the following buckets for ascertaining the Gap in individual buckets and the cumulative Gap.

- a. 1 day to 14 days
- b. 14 days to 1 month
- c. Over 1 month to 2 months
- d. Over 2 months to 3 months
- e. Over 3 months to 6 months
- f. Over 6 months to 1 year
- g. Over 1 year to 3 years
- h. Over 3 to 5 years
- i. Over 5 years

The reporting format ALM-3 will be used for computing gaps in each time bucket. Within each time bucket, there could be mismatch depending on interest rate sensitive cash inflows and outflows. The Management Committee or such other Committee as may be authorized by the Board in this regard, shall set Prudential Limits on Individual Gaps within each time bucket, as defined earlier in this section, considering Total Assets, Earning Assets, Equity or Interest Rate Movements, etc.

## 10. Reporting to RBI

In view of the possibilities of leveraged investments, and asset liability mismatches resulting from use of short term sources to fund ICF activities, a system of reporting will be followed. The return will comprise of:

- (i) Statement of short-term dynamic liquidity [NBS-ALM1],
- (ii) Statement of structural liquidity [NBS-ALM2] and
- (iii) Statement of Interest Rate Sensitivity [NBS-ALM3].

The periodicity of the Statement of short-term dynamic liquidity [NBS-ALM1] shall be quarterly and that of Statement of structural liquidity [NBS-ALM2] and Interest Rate Sensitivity [NBS-ALM3] shall be half yearly. Quarterly Statement(s) shall be submitted within 15 days of the close of the quarter to which it relates and half yearly statement(s) within 30 days of the close of the half year to which it



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relates, to the Regional Office of the Department in whose jurisdiction, ICF is registered. Operational Group will review and approve the same for submission to RBI.

## 11. ALCO Committee:

ALCO committee consist of below two persons from the board and same is approved by the Board of Directors of the Company:

1. Radha Kapoor Khanna
2. Roshini Kapoor



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